

CITY OF ASHEVILLE
MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2005

As management of the City of Asheville, we offer readers of the City of Asheville's financial statements this narrative overview and analysis of the financial activities of the City of Asheville for the fiscal year ended 2005. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in the City's Notes to the Financial Statements, which follow this narrative.

FINANCIAL HIGHLIGHTS

- The assets of the City of Asheville exceeded its liabilities at the close of the most recent fiscal year by \$308,825,039 (*net assets*). Of this amount, \$53,781,122 (*unrestricted net assets*) may be used to meet the government's ongoing obligations to citizens and creditors.
- The City's total net assets increased by \$3,489,206.
- As of the close of the current fiscal year, the City of Asheville's governmental funds reported combined ending fund balances of \$37,341,680 an increase of \$1,693,606 in comparison with the prior year. Approximately 48% or \$17,835,166 is *available for spending* at the government's discretion (*unreserved fund balance*).
- At the end of the current fiscal year, unreserved fund balance for the general fund was \$17,275,784, or 25% of total general fund expenditures.
- The City's total long-term liabilities decreased by \$7,684,769 during the current fiscal year. The key to this decrease is attributable to the normal pay down of existing debt.
- The City holds the following bond ratings:

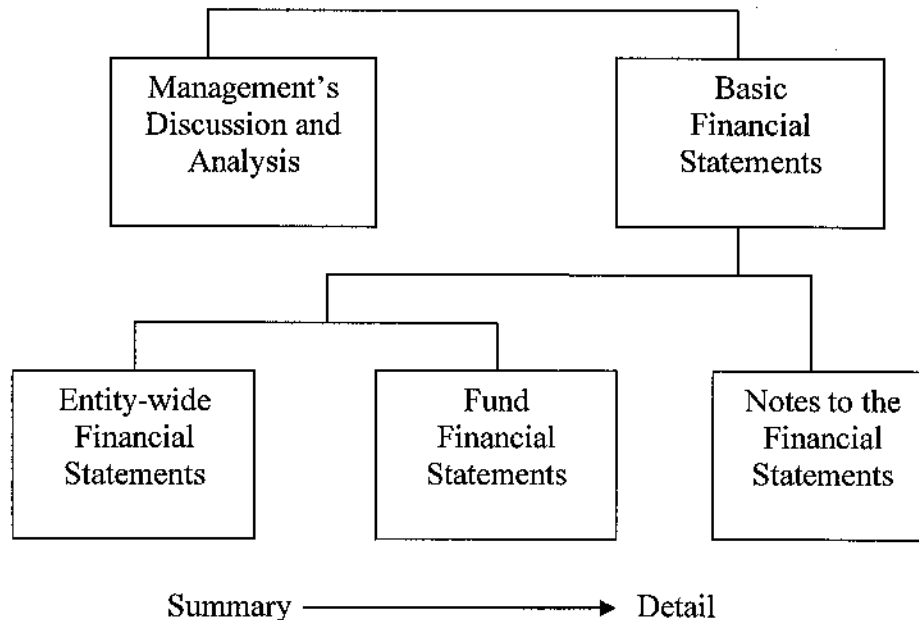
Moody's	Aa2
Standard & Poor's	AA

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the City of Asheville's basic financial statements. The City of Asheville's basic financial statements are comprised of three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves and the compliance section containing information required by Government Auditing Standards, Office of Management and Budget (OMB) Circular A-133 and the North Carolina Single Audit Implementation Act.

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Required Components of Annual Financial Report



Basic Financial Statements

The first two statements (Exhibit A & B) in the basic financial statements are the **Government-wide Financial Statements**. They provide both short and long-term information about the City's financial status.

The next statements (Exhibits C through J) are **Fund Financial Statements**. These statements focus on the activities of the individual components of the City's Government. These statements provide more detail than the government-wide statements. There are three parts to the Fund Financial Statements: 1) the governmental fund statements, 2) the proprietary fund statements, and 3) the fiduciary fund statement.

The next section of the basic financial statements is the **Notes to the Financial Statements**. The notes explain in detail some of the data contained in those statements. The **Required Supplemental Information** contains additional information required by accounting principles generally accepted in the United States of America. After the notes and the required supplemental information, additional **Supplemental Information** is provided. The other supplemental information shows details about the City's individual funds, including budgetary information required by the North Carolina General Statutes, as well as other data that the City considers helpful to the reader.

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Government-wide Financial Statements. The *government-wide financial statements* are designed to provide readers with a broad overview of the City of Asheville's finances, in a manner similar to a private-sector business. The government-wide statements provide short and long-term information about the City's financial status as a whole.

The *statement of net assets* presents information on all of the City of Asheville's assets and liabilities, with the difference between the two reported as *net assets*. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the City of Asheville is improving or deteriorating.

The *statement of activities* presents information showing how the government's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, *regardless of the timing of related cash flows*. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods (e.g., uncollected taxes and earned but unused vacation leave).

Both of the government-wide financial statements distinguish functions of the City of Asheville that are principally supported by taxes and intergovernmental revenues (*governmental activities*) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (*business-type activities*). The governmental activities of the City of Asheville include General Government, Public Safety, Highways and Streets, Environmental Protection, Economic Development, and Culture and Recreation. The business-type activities of the City of Asheville include Water Resources, Civic Center, Festivals, Parking Services and Mass Transit.

The government-wide financial statements include not only the City of Asheville itself (known as the *primary government*), but also the legally separate Asheville Board of Alcoholic Control (known as the *component unit*). Financial information for this *component unit* is reported separately from the financial information presented for the primary government itself. The government-wide financial statements are Exhibit A and B of this report.

Fund Financial Statements. A *fund* is a grouping of related accounts that are used to maintain control over resources that have been segregated for specific activities or objectives. The City of Asheville, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements, such as the general statutes or the City's Budget Ordinance. All of the funds of the City of Asheville can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds. Experienced readers of governmental financial statements will find these financial statements most familiar.

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Governmental Funds. *Governmental funds* are used to account for essentially the same functions reported as *governmental activities* in the entity-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on *near-term inflows and outflows of spendable resources*, as well as on *balances of spendable resources* available at the end of the fiscal year. Such information may be useful in evaluating the City's near-term financing requirements. Governmental funds are reported using an accounting method called modified accrual accounting, which provides a conservative short-term spending focus. As a result, the governmental fund financial statements give the reader a detailed short-term view that helps him or her determine if there are more or less financial resources available to finance the City's programs.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for *governmental funds* with similar information presented for *governmental activities* in the entity-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet (Exhibit C) and the governmental fund statement of revenues, expenditures, and changes in fund balances (Exhibit D) provide a reconciliation to facilitate this comparison between *governmental funds* and *governmental activities*. (Exhibit C & E)

The City of Asheville maintains ten individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the General Fund. Data from the other nine governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these non-major governmental funds is provided in the form of *combining statements* elsewhere in this report.

The City of Asheville adopts an annual appropriated budget for its General Fund as required by General Statute. A budgetary comparison statement has been provided for the General Fund to demonstrate compliance with this budget. (Exhibit F)

Proprietary Fund. The City of Asheville maintains one type of proprietary fund. *Enterprise funds* are used to report the same functions presented as *business-type activities* in the entity-wide financial statements. The City of Asheville uses enterprise funds to account for its Water resources, Civic Center, Festivals, Parking Services and Mass Transit Operations. The City has no internal service funds.

Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. The proprietary fund financial statements provide separate information for the Water Resources Fund, which is considered to be a major fund of the City of Asheville. The basic proprietary fund financial statements can be found on Exhibit G through I of this report.

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Fiduciary Funds: Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are *not* reflected in the government-wide financial statement because the resources of those funds are *not* available to support the City of Asheville's own programs. The accounting used for fiduciary funds is much like that used for proprietary funds. The City of Asheville maintains one agency fund, which is its only fiduciary fund. The basic fiduciary fund financial statement can be found on Exhibit J of this report.

Notes to the Basic Financial Statements: The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements are on pages 30-61 of this report.

Other Information: In addition to the basic financial statements and accompanying notes, this report also presents certain *required supplementary information* concerning the City of Asheville's progress in funding its obligation to provide pension benefits to its employees. Required supplementary information can be found on pages 62-63 of this report. The combining statements referred to earlier in connection with non-major governmental funds are presented immediately following the required supplementary information on pensions.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

The Government-wide financial statements are designed to provide the reader with a broad overview of the City's finances, similar in format to a financial statement of a private-sector business. The government-wide statements provide short and long-term information about the City's financial status as a whole. The two government-wide statements report the City's net assets and how they have changed. Net assets are the difference between the City's total assets and total liabilities. Measuring net assets is one way to gage the City's financial condition.

As noted earlier, net assets may serve over time as a useful indicator of a government's financial condition. In the case of the City of Asheville, assets exceeded liabilities by \$308,825,039 as of June 30, 2005.

By far the largest portion of the City's net assets (\$249,270,370 or 80%) reflects the City's investment in capital assets (e.g., land, buildings, infrastructure, machinery, and equipment), less any related debt that is still outstanding that was issued to acquire those assets. The City of Asheville uses these capital assets to provide services to citizens; consequently, these assets are *not* available for future spending. Although the City of Asheville's investment in its capital assets is reported net of the outstanding related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets are committed to the continued provision of service and cannot be used to liquidate these liabilities.

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	Governmental Activities		Business-type Activities		Total	
	2004	2005	2004	2005	2004	2005
Current and Other Assets	\$ 44,273,366	\$ 46,834,443	\$ 30,828,402	\$ 31,649,565	\$ 75,101,768	\$ 78,484,008
Capital Assets	200,337,934	192,590,745	132,503,328	134,506,297	332,841,262	327,097,042
Total Assets	244,611,300	239,425,188	163,331,730	166,155,862	407,943,030	405,581,050
Non-current Liabilities	35,614,904	31,306,131	57,769,138	54,450,879	93,384,042	85,757,010
Other Liabilities	4,383,094	5,054,344	5,494,790	5,944,657	9,877,884	10,999,001
Total Liabilities	39,997,998	36,360,475	63,263,928	60,395,536	103,261,926	96,756,011
Net Assets:						
Invested in Capital Assets, Net of						
Related Debt	173,149,100	168,990,305	75,086,520	80,280,065	248,235,620	249,270,370
Restricted	5,750,559	5,773,547	-	-	5,750,559	5,773,547
Unrestricted	25,713,643	28,300,861	24,981,282	25,480,261	50,694,925	53,781,122
Total Net Assets	\$204,613,302	\$203,064,713	\$100,067,802	\$105,760,326	\$304,681,104	\$308,825,039

Of the total net assets for the City of Asheville, 66% represent net assets involved in governmental activities such as street related infrastructure.

The remainder of net assets reflects business-like activities. At the end of the current fiscal year, the City of Asheville is able to report positive balances in all three categories of net assets, both for the government as a whole, as well as for its separate governmental and business-type activities. The same situation held true for the prior fiscal year.

In addition, total unrestricted net assets amounted to 19% of total net assets. Unrestricted net assets may be used to meet the government's ongoing obligation to citizens and creditors.

The City's net assets increased by \$3,489,206 during the current fiscal year. The increase is due in large part to increases in operating grants, taxes received and investment earnings.

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City of Asheville's Net Assets

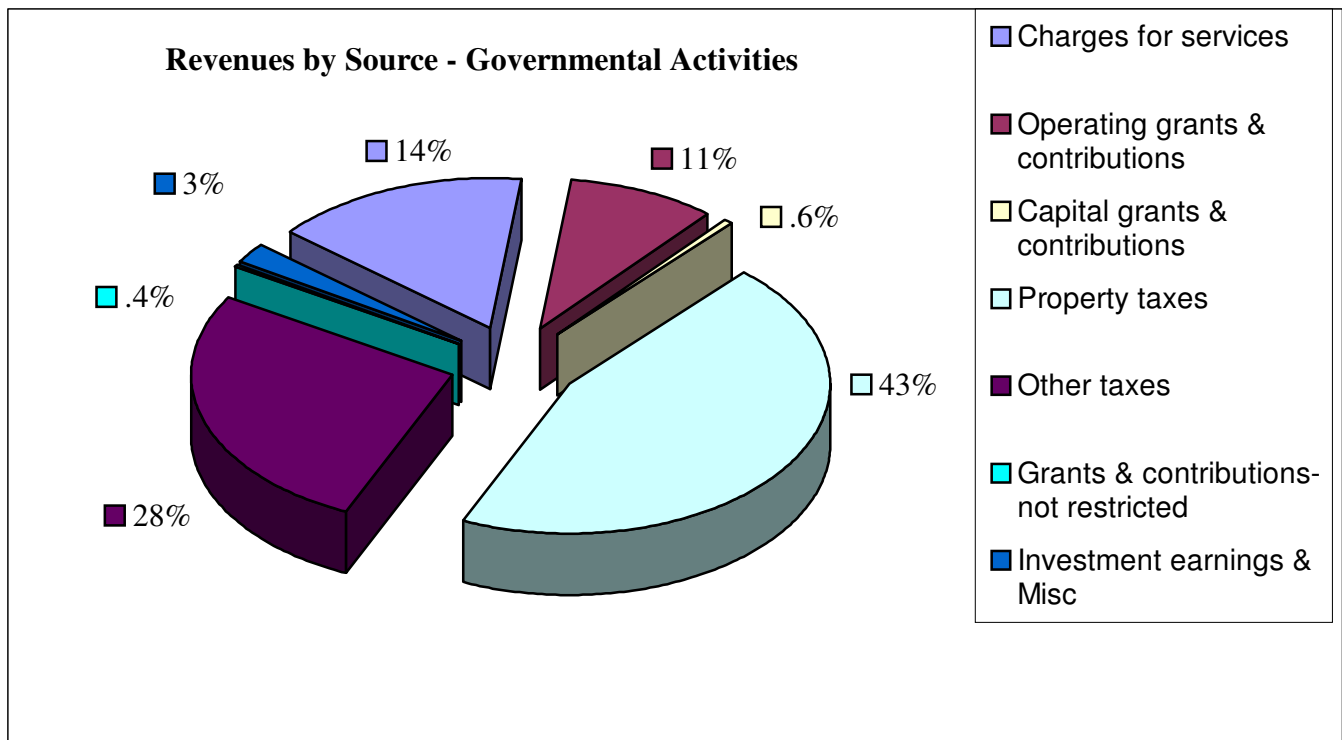
	Governmental Activities		Business-type Activities		Total	
	2004	2005	2004	2005	2004	2005
Revenues:						
Program revenues:						
Charges for services	\$ 12,007,123	\$ 11,602,482	\$ 27,805,317	\$ 28,864,108	\$ 39,812,440	\$ 40,466,590
Op. grants & contributions	6,786,553	9,553,135	1,883,705	2,501,146	8,670,258	12,054,281
Cap Grants & contributions	462,736	346,387	2,076,882	2,164,652	2,539,618	2,511,039
General revenues:						
Property taxes	33,946,832	35,078,520	-	-	33,946,832	35,078,520
Other taxes	20,227,352	22,802,059	-	-	20,227,352	22,802,059
Grants & contributions not						
restr'd to spec programs	289,636	222,192	-	-	289,636	222,192
Inv earnings & misc	1,680,142	2,504,354	740,810	34,549	2,420,952	2,538,903
Total Revenues	\$ 75,400,374	\$ 82,109,129	\$ 32,506,714	\$ 33,564,455	\$107,907,088	\$115,673,584
Expenses:						
General government	21,148,189	14,782,234	-	-	21,148,189	14,782,234
Public Safety	30,513,376	31,479,913	-	-	30,513,376	31,479,913
Highway/streets	5,650,832	22,398,691	-	-	5,650,832	22,398,691
Env Protection	5,024,914	-	-	-	5,024,914	-
Econ Development	3,533,572	5,181,004	-	-	3,533,572	5,181,004
Culture and recreation	5,119,628	7,347,525	-	-	5,119,628	7,347,525
Int on long-term debt	1,340,737	1,181,798	-	-	1,340,737	1,181,798
Water resources	-	-	20,623,941	21,093,595	20,623,941	21,093,595
Civic Center	-	-	2,668,573	2,360,809	2,668,573	2,360,809
Festivals	-	-	1,121,437	1,067,019	1,121,437	1,067,019
Parking Services	-	-	1,347,655	1,363,805	1,347,655	1,363,805
Mass Transit	-	-	3,775,388	3,927,985	3,775,388	3,927,985
Total Expenses	\$72,331,248	\$ 82,371,165	\$ 29,536,994	\$ 29,813,213	\$101,868,242	\$112,184,378
In/decrease in net assets						
before transfers	3,069,126	(262,036)	2,969,720	3,751,242	6,038,846	3,489,206
Transfers	(1,883,441)	(1,941,282)	1,883,441	1,941,282	-	-
In(decrease) in net assets	1,185,685	(2,203,318)	4,853,161	5,692,524	6,038,846	3,489,206
Net assets, beginning						
of year, restated	203,427,617	205,268,031	95,214,641	100,067,802	298,642,258	305,335,833
Net assets, end of year	\$204,613,302	\$203,064,713	\$100,067,802	\$105,760,326	\$304,681,114	\$308,825,039

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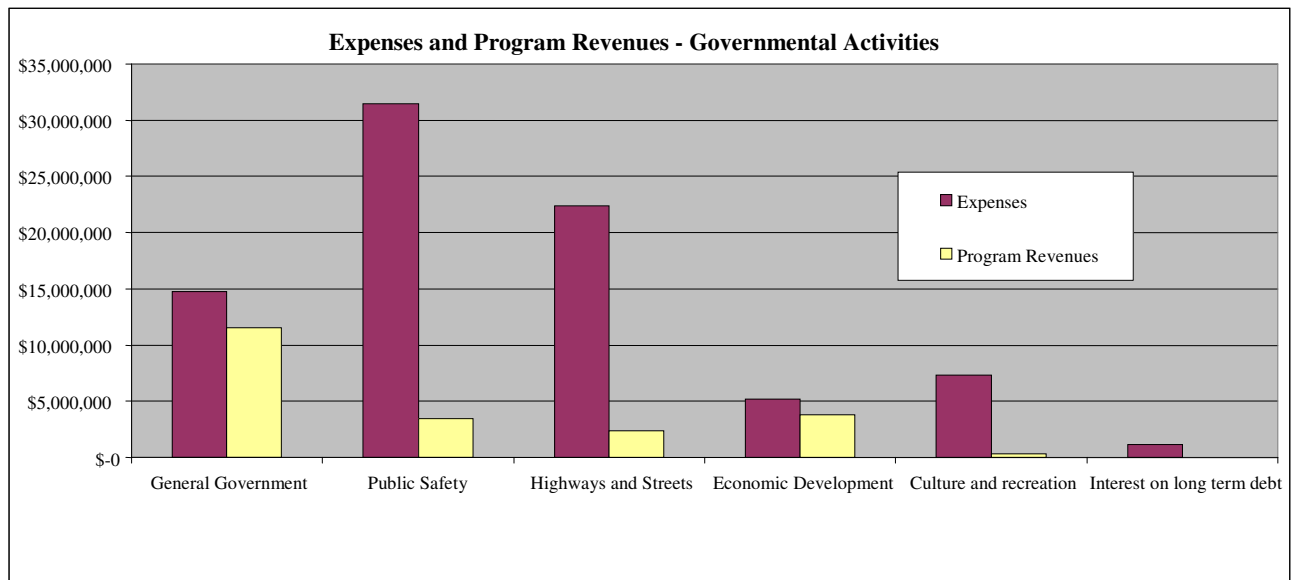
Governmental activities. Governmental activities decreased the City of Asheville's net assets by \$2,203,318. Key elements of this reduction from prior year are as follows:

- Operating grants for governmental activities increased by \$2,766,582, mostly as a result of an aggressive grant application undertaken by the City during the current fiscal year. The new grant awards furnished resources to support three of the City's functions: public safety, highways/streets and culture and recreation.
- Property taxes increased by \$561,909 during the year. Most of this increase is the product of tax base growth from new construction and annexation.

For the most part, increases in expenses closely parallel inflation and growth in the demand for services. Two noteworthy exceptions however, were Highways/streets (\$11,722,945) and Culture/recreation (\$2,227,897). These two areas bore most of the responsibility for the governmental activities, in repairing the damages caused by Hurricanes Frances and Ivan's devastating blow to the City of Asheville.



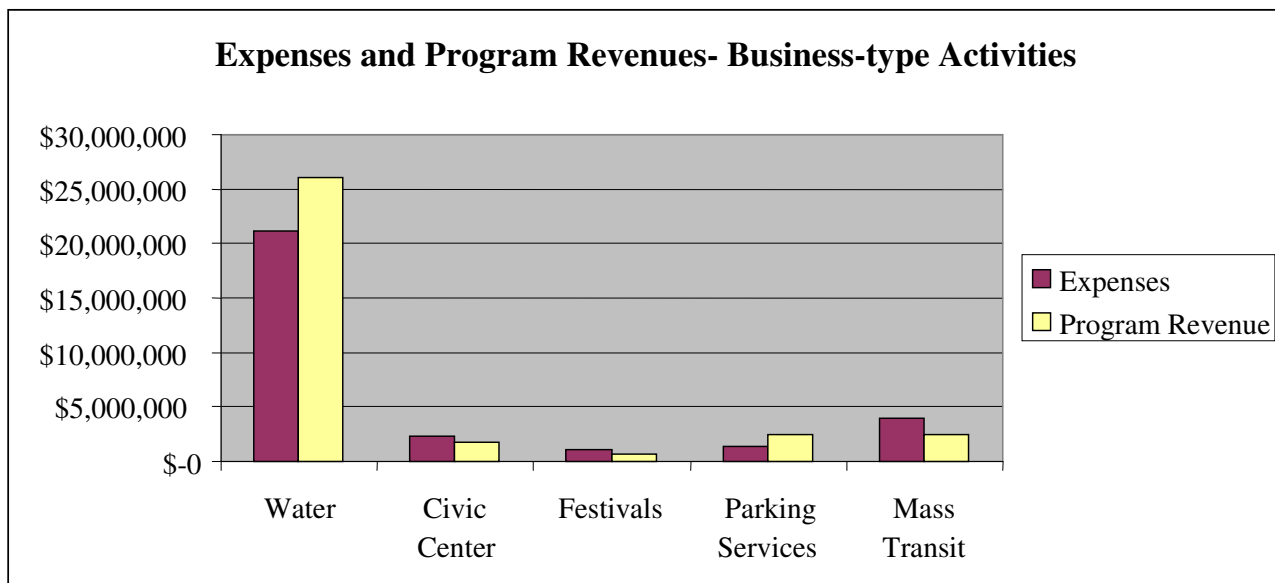
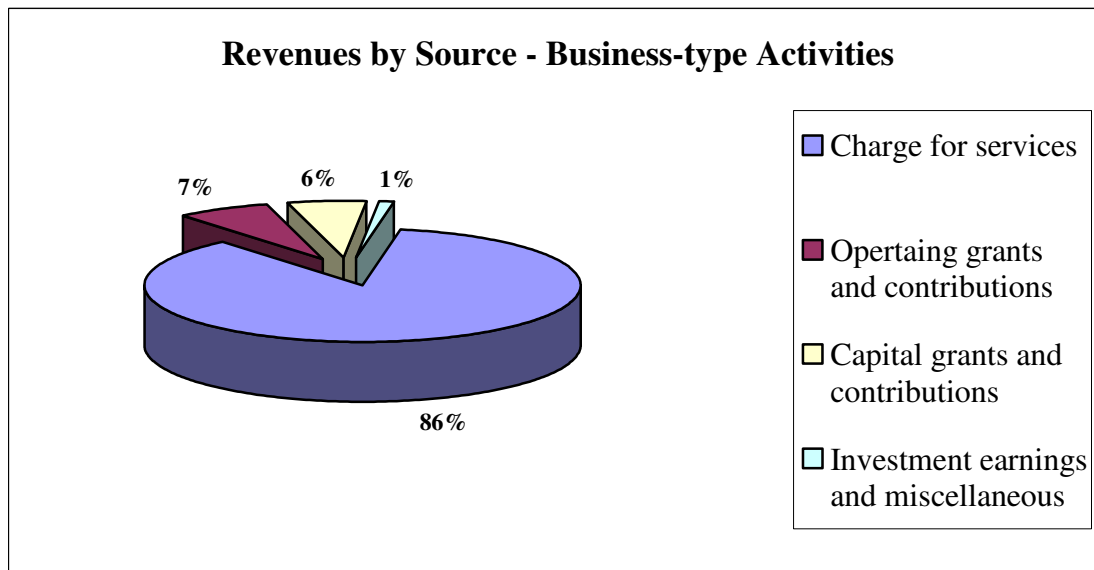
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Business-type activities. Business-type activities increased the City of Asheville's net assets by \$5,692,524. Key elements of this increase are as follows:

- Charges for services for business-type activities increased by 3.8% to \$28,864,108 due to increased demand for services.
- Operating grants and contributions increased by 32.7% to \$2,501,146 due to active solicitation of grants.
- Capital grants and contributions increased by 4.2% to \$2,164,652 due to state issued grants for water improvements and mass transit services.

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Financial Analysis of the City's Funds

As noted earlier, the City of Asheville uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

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Governmental Funds. The focus of the City of Asheville's *governmental funds* is to provide information on near-term inflows, outflows, and balances of *spendable* resources. Such information is useful in assessing the City of Asheville's financing requirements. In particular, *unreserved fund balance* may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

As of the end of the current fiscal year, the City of Asheville's governmental funds reported combined ending fund balances of \$37,341,680, an increase of \$1,693,606 from the prior year. More than half of this total amount (\$17,835,166) constitutes *unreserved fund balance*, which is available for spending at the City's discretion. The remainder of the fund balance is *reserved* to indicate that it is not available for spending. Reserved fund balance includes \$2,486,450 committed to liquidate contracts and purchase orders that remain unperformed at year-end, \$7,913,428 reserved as required by North Carolina General Statute 159.8(a), \$2,491,093 reserved for the City's affordable housing program, \$5,768,547 committed to process health benefits, \$5,000 for maintenance of the City's cemetery and \$841,996 that is restricted by Statute for a variety of other purposes.

The General Fund is the chief operating fund of the City of Asheville. At the end of the current fiscal year, unreserved or undesignated fund balance of the General Fund was \$17,275,784, while total fund balance was \$32,804,575. As a measure of the General Fund's liquidity, it may be useful to compare both unreserved and undesignated fund balance and total fund balance to total fund expenditures. Unreserved and Undesignated fund balance represents 25% of total General Fund expenditures, while total fund balance represents 48% of that same amount.

The fund balance of the City of Asheville's General Fund increased by \$2,216,559 during the current fiscal year. Key factors in this growth are as follows:

- Ad valorem tax revenues increased approximately \$561,909, as a result of an increase in the tax base due to annexation and normal construction activity and a collections rate of 99%.
- Local sales tax revenues increased by \$983,816. This is due in part to a steady growth in tourism and retail sales.
- Intergovernmental revenues of the general fund increased by \$993,020 as a result of an increase in state shared revenues.
- The increase in the General Fund expenditures of \$6,213,186 reflects the impact Hurricanes Francis and Ivan had on the City.

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Proprietary Funds: The City of Asheville's proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail. Unrestricted net assets of the Proprietary funds at the end of the year amounted to \$25,480,261. The total growth in net assets for the funds was \$5,692,524. The increase in net assets is due in part to the pay down of debt and increases in fixed assets of the water system financed in part by state grants.

General Fund Budgetary Highlights

During fiscal 2005, there was a \$2,880,858 increase in appropriations between the original and final amended budget of expenditures. Some of the components of that increase were:

- \$77,500 appropriated from fund balance to various departments for FSLA mandated overtime expenses;
- \$63,548 appropriated to the Parks & Recreation department to fund operations at the Aston Park tennis facility, which reverted to the City from Buncombe County;
- \$425,000 appropriated from fund balance for the purchase of equipment for URTV;
- \$765,000 in stop-loss insurance recovery revenue appropriated to cover health care expenditures;
- \$599,610 in reimbursement revenue from FEMA appropriated for expenses incurred during the flood events of September 2004;
- \$85,000 appropriated from fund balance to the Parks & Recreation department for the purchase of various pieces of equipment.

Ad valorem taxes exceeded budget expectations with the assessed valuation of real property increasing by 3.5%. Local option sales tax revenue increased by 7.1% in fiscal year 2005 and exceeded budget by \$485,835. The other major General Fund revenue categories – intergovernmental and charges for services – also exceeded budget estimates.

Capital Asset and Debt Administration

Capital assets. The City of Asheville's investment in capital assets for its governmental and business type activities as of June 30, 2005 amounts to \$327,097,042 (net of accumulated depreciation). This investment in capital assets includes land, buildings and improvements, water and sewer system, machinery and equipment, park facilities, roads, highways, bridges, curbs and gutters, sidewalks and stormwater. The City of Asheville's net investment in capital assets decreased \$5,744,220 because current year depreciation expense exceeded current year capital asset additions.

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City of Asheville's Capital Assets

	Governmental Activities		Business-type Activities		Total	
	2004	2005	2004	2005	2004	2005
Land	\$ 20,192,831	20,620,738	\$ 9,158,238	\$ 9,158,238	\$ 29,351,069	\$ 29,778,976
Buildings & Improvements	39,096,666	39,181,060	77,972,923	79,450,212	117,069,589	118,631,272
Machinery & Equipment	24,780,456	26,736,590	12,084,755	12,386,069	36,865,211	39,122,659
Infrastructure	216,143,023	216,220,372	87,114,575	91,642,758	303,257,598	307,863,130
Construction In Process	4,730,071	6,508,303	4,306,879	4,183,876	9,036,950	10,692,179
Accumulated Depreciation	(104,605,113)	(116,676,318)	(58,134,042)	(62,314,856)	(162,739,155)	(178,991,174)
Total	\$ 200,337,934	\$ 192,590,745	\$ 132,503,328	\$ 134,506,297	\$ 332,841,262	\$ 327,097,042

Additional information on the City's capital assets can be found in Note 4 of this report.

Long-term debt. At the end of the current fiscal year, the City of Asheville had total bonded debt outstanding of \$15,395,000, all of which is backed by the full faith and taxing authority of the City. The remainder of the City of Asheville's bonded debt represents bonds secured solely by specified revenue sources (i.e., revenue bonds).

City of Asheville's Outstanding Debt
General Obligation and Revenue Bonds

	Governmental Activities		Business-type Activities		Total	
	2004	2005	2004	2005	2004	2005
General Obligation bonds	\$ 9,101,212	\$ 7,675,887	\$ 9,289,473	\$ 7,719,113	\$ 18,390,685	\$ 15,395,000
Revenue bonds	-	-	44,090,000	42,960,000	44,090,000	42,960,000
Total	\$ 9,101,212	\$ 7,675,887	\$ 53,379,473	\$ 50,679,113	\$ 62,480,685	\$ 58,355,000

The City of Asheville's total general obligation and revenue bonds debt decreased by \$4,125,685 (6.6%) during the current fiscal year in accordance with its regularly scheduled maturity dates. The City did not issue any new general obligation or revenue bonds.

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The City of Asheville maintains an "AA" rating from Standard & Poor's and an "Aa2" rating from Moody's for general obligation debt. This bond rating is a clear indication of the sound financial condition of the City.

State statutes limit the amount of general obligation debt a governmental entity may issue to 8% of its total assessed value of taxable property located within that government's boundaries. The legal debt margin for the City of Asheville is \$518,900,666, which is significantly in excess of the City of Asheville's outstanding general obligation debt. Additional information regarding the City of Asheville's long-term debt can be found in Note 7 of this report.

Economic Factors and Next Year's Budgets and Rates

- The unemployment rate for the City of Asheville is currently 4.6%, which is a slight increase from a rate of 4.5% a year ago. This compares favorably to the state's average unemployment rate of 5.0%.
- Population of 73,739 has grown 8.7% from 1995 to 2005.
- Inflationary trends in the region compare favorably to national indices.

All of these factors were considered in preparing the City of Asheville's budget for the 2006 fiscal year.

During the current fiscal year, unreserved fund balance in the general fund increased to \$17,275,784. The City of Asheville has appropriated \$50,000 of this amount for the purchase of television equipment. This appropriation will come out of PEG (Public Educational & Government) fees, which are paid to the City by the local cable company in support of the public educational and government access channels.

Budget Highlights for the Fiscal Year Ending June 30, 2006.

The City's adopted General Fund budget for FY 2006 totaled \$74,357,126, which represents a 3.4% increase over the FY 2005 budget. Police and Fire expenditures continue to be the largest component of the City's General Fund budget comprising approximately 39% of the total FY 2006 General Fund budget. The FY 2006 budget includes \$292,710 to fund five new police officers to enhance drug enforcement efforts in the City. The budget also includes \$70,000 to fund higher fuel costs for police and fire vehicles. The General Fund budget also includes \$2.3 million in pay-as-you-go capital improvement funding. This funding will allow the City to continue replacing its aging fleet of vehicles and undertake several other high priority projects, including renovations at the Reid and Montford recreation centers and the replacement of the East Oakview bridge. The fiscal year 2006 General Fund budget includes \$6.14 in debt service for the City's general obligation bonds, certificates of participation (COPs), and other general debt obligations. Debt service for FY 2006

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increased slightly compared to the prior year due to the planned issuance of \$2.8 million in COPs to fund the construction of a new fire station.

Business-type Activities: The FY 2006 budget for the Water Resources Fund maintains current water rates with the assumption that there will be no growth in demand. The Water Resources Fund's overall budget shows an increase of only 1.7% in FY 2006 when compared to the prior year. The Water Resource capital budget totals \$3.41 million and includes funding for capital improvement projects, an aggressive meter change-out program, rolling stock, and small capital equipment. Water Resources' debt service for FY 2006, which is 23% of the total budget, includes debt service for the 1992 General Obligation Bonds, the 1996 NC Water Quality Loan, Series 1996 Revenue Bonds, and Series 2001 Revenue Bonds. The FY 2006 budget also includes a new business-type activity, the Stormwater Utility Fund, which was created to account for the expenses associated with the City's efforts to meet federally mandated stormwater requirements.

Requests for information

This financial report is designed to provide a general overview of the City of Asheville's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Office of the Chief Financial Officer, City of Asheville, PO Box 7148, Asheville NC 28802.

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